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FAIR TRADE IS COUNTERPRODUCTIVE AND UNFAIR: REJOINDER

Colleen Haight and David R. Henderson

This is a rejoinder to a criticism of Henderson (2008) by Alastair Smith. Our conclusion is that Henderson's basic case, although nicked around the edges by developments since the original was written, still stands. Moreover, we point out that Smith's criticism of Henderson's point that Fair Trade could help kill the banana actually supports Henderson's case. Finally, Smith's proposed 'trade, not aid' solution does not contradict Henderson (2008). Refusing to buy Fair Trade coffee and other products and, instead, buying quality coffee and other products would not reduce trade, as Smith seems to imply.

Keywords: Fair trade, labour standards, free trade.

Introduction

In his response to Henderson (2008), Alastair Smith (2009) makes a number of theoretical and factual claims about both Fair Trade¹ and Henderson (2008). We agree with a few of these claims and disagree with many. One of the authors, Haight (formerly Berndt), did substantial field work in Central America on the issue of Fair Trade in coffee, which is why she is a co-author of this article. The other, Henderson, wrote the original article to which Mr Smith responded. We examine, *seriatim*, both Mr Smith's own claims and his criticisms of Henderson. Our conclusion is that Henderson's basic case, although nicked around the edges by Mr Smith and, more importantly, by developments since the original was written, still stands.

Labour standards

The first substantive claim with which Mr Smith takes issue is Henderson's statement that Fairtrade Labelling Organization (FLO) certification 'has only little to do with how it treats its employees'. Mr Smith writes: '[T]he sections covering Labour Conditions are in fact one of the most detailed and considered'. While it is true that there are standards, monitoring of compliance is sporadic, according to Michael Keaton of Transfair.² Moreover, the protections that Fair Trade offers are redundant. Both Costa Rica and Guatemala have laws in place. In many cases,

just as for Fair Trade rules, the laws are only intermittently enforced.

Mr Smith states:

'far from taking labour conditions lightly, FLO standards are based on those advocated by the conventions of the International Labour Organization (FLO, 2009, p. 23). In operationalising this, FLO has embedded around 1,100 words on labour standards (compared with the 600-odd words covering Social Development of which the issue of co-operatives, apparently so strongly emphasised, is but one small section) in its Generic Standards and set detailed requirements in the areas of: employment policy; freedom from discrimination; freedom of labour; freedom of association and collective bargaining; conditions of employment; and occupational health and safety.'

Mr Smith continues:

'In contrast to other established labour codes, these are largely not only applicable to full-time workers, but in fact to "all waged employees of the producer organization and of its members . . . [which] includes migrant, temporary, seasonal, sub-contracted and permanent workers" (FLO, 2009, p. 24).'

The document to which Mr Smith refers was last revised on 1 January 2009. Of the document's 31 pages, seven are devoted to labour conditions (as opposed to 11 for environmental development, the longest section). The opening paragraph lays out the

expectation that organisations meet the standards of the International Labour Organization, but does not describe entirely what those requirements might be. Later in the standards, however, certain sections of the ILO conventions are specifically mentioned, leading a reasonable reader to think that the important provisions of the ILO are presented within the document and that one need not consult the ILO further.

The preamble to the sections also points out that '[t]he focus of the compliance criteria as set by the certifier will be on the permanent workers' (p. 24 of 'Generic Standards for Small Producers' Organizations'). Because Fair Trade regulations as they pertain to coffee farms restrict members to only those family-owned and family-operated farms that are 'not structurally dependent on permanent hired labour' (p. 4), the seasonal labourers who harvest the coffee are clearly *not* the focus of the compliance criteria.

The first section of labour standards in this document gives direction as to how to devise an employment policy, while also specifying that there are no minimum requirements for an employment policy (p. 24). Indeed, nowhere does it specify that an employment policy is required. The second section pertains to discrimination and sets out a comprehensive list of those who constitute the 'protected class'. The protected classes include not only those protected by US law, but also such categories as 'social origin' and 'political opinion'. The third section prohibits the use of forced labour and child labour. The fourth provides for collective bargaining agreements. It is only in the fifth and sixth sections that one finds an outline of conditions of employment and safety.

One immediately notices in the section on conditions of employment the provisions for wages, sick leave and overtime. However, the fine print in each section suggests that the organisation must comply with minimum-wage laws or, where no such laws exist, must follow the industry standard. In other words, Fair Trade provides for nothing new. The regulations only echo those provisions already in place at the national and industry level. The fact that Fair Trade firms must comply with industry-level norms is significant, given that Fair Trade-certified farms and co-operatives do *not* represent the majority of producers in any Central American country. In fact, by volume, Fair Trade coffee is just over 2% of the coffee produced in Guatemala, the largest coffee-producing country in Central America. In other words, Fair Trade firms must comply with standards already set by an industry that is not comprised mainly of Fair Trade firms. The safety requirements are similarly impotent. They speak of 'adequate' safety training, 'adequate' safety equipment, and working conditions that are 'as safe as reasonably practicable'. (pp. 30–31). Such relative terms leave the door wide open to interpretation and limit any organisation's ability to measure compliance.

These standards are the Generic Standards. However, there are also standards specific to certain products, such as coffee and bananas. These standards do not mention employment conditions, but, instead, focus on contracting guidelines for the sale and export/import requirements.

Mr Smith writes:

'More recently the FLO has also revised the definition of a "small producer" to further ensure that producer realities are accurately

reflected in their Generic Standards. Two definitions are now offered with one being applied to product categories that (1) *are not* (highly) labour dependent and (2) *are* (highly) labour dependent (FLO, 2009, p. 4). In the second category it is now explicitly acknowledged that farmers have the option to hire non-family labour so long as, "The number of permanent hired workers does not exceed a specific factor per hectare per crop, as defined by the certification body in its compliance criteria" (FLO, 2009, p. 4). This means that while governance encourages family-based entrepreneurship, it accepts that in some situations, some families may need to make other provisions.'

Mr Smith is making our case. He points out, in his own footnote 7, that coffee is in the first category; in other words, coffee is in the category for which it is *not* explicitly acknowledged that farmers may hire non-family labour.

Co-operatives

Mr Smith writes:

'Henderson writes that "a substantial amount of the gains from the Fairtrade price *are eaten up by the co-operative bureaucracy*". While it is not factually incorrect that a portion of the Fairtrade price remains with the co-operative (and indeed that the Fairtrade price is guaranteed to the first co-operative level only, and not to individual farmers), I wonder why this must be described as being "eaten up by bureaucracy", and not perhaps, "absorbed in administrative and investment costs"? (emphasis in original).

Because we see this as purely a semantic issue, we accept Mr Smith's change in wording.

Mr Smith points out, correctly, that the citation Henderson offered to back up his claim about the gains being eaten up by bureaucracy lead to 'no relevant information on the page indicated'. We apologise for the incorrect citation. The correct citation is: Colleen E. H. Berndt, 'Is Fair Trade in Coffee Production Fair and Useful? Evidence from Costa Rica and Guatemala and Implications for Policy', *Mercatus Policy Series, Policy Comment No. 11*, June 2007, p. 23. In it, Berndt writes:

'Does Fair Trade make a difference to the lives of the small farmer through its premiums and pre-financing? According to the FLO, the answer is an unqualified yes. "Fair Trade certification empowers farmers and farm workers to lift themselves out of poverty." The FLO's web site offers producer profiles, detailing, for example, how farmers in Huehuetenango, Guatemala, are given scholarships to send their children to school. Fedecocagua, the largest Fair Trade certified cooperative in Guatemala, says this is not the whole story. "The premium we use here [at the cooperative] . . . you saw our coffee lab, it is very professional . . . But if I tried to give you the five cents from the Fair Trade, just for you [meaning the small farmer], probably it's nothing."³ The representative went on to say that many organizations come to Guatemala, build a school or clinic, and then take pictures for their Web sites. In his experience, this was not a normal benefit of Fair Trade.'

Mr Smith states:

'This efficiency critique also fails to appreciate that costs to invest in Fairtrade certification are, in effect, voluntarily undertaken by producers. FLO merely acts as an intermediary. Those responsible for

their decisions, in effect, contribute towards a continual cost–benefit analysis and if no gains are seen, or discovered over time, individuals and indeed whole organisations are free to reject certification. In this way, simply quoting the cost of certification for co-operatives is irrelevant to an evaluation of the system without a co-nsideration of either the returns available to individual co-operatives/farmers, or the way that such licensing fees are subsequently spent by the FLO.’

We agree that people voluntarily undertake these actions. Henderson (2008) did not state otherwise. His goal, and our goal, is to inform the various participants so that they can make good decisions.

Direct assistance or trade?

Henderson (2008) pointed out that people in richer countries could better help people in poor countries by taking the extra amount they would have spent on Fair Trade products and giving it directly to those people. Mr Smith argues that trade is better than aid and cites Adam and O’Connell (2004). There are two problems with his citation of that article. Firstly, Adam and O’Connell present a possibility theorem and a simulation; they give no evidence. Secondly, even if trade is better than aid, something that is plausible and probably true, that is irrelevant to this debate. Henderson (2008) did not advocate less trade: people who buy coffee will continue to buy coffee. Rather, he argued against Fair Trade – that is, paying a higher price for coffee produced under particular conditions. Indeed, he agrees with the previously cited Berndt (2007) that purchasing speciality coffee, rather than coffee produced under particular Fair Trade conditions, benefits producers:

‘Because of the nature of specialty coffee cultivation, entrepreneurs who engage in the high-quality production that consumers demand need to pay high wages to attract skilled and efficient labor. By focusing on quality, coffee outlets such as Allegro, Peet’s, and Starbucks are in fact encouraging development and socially conscious business practices through entrepreneurship. While this does not replace a faulty institutional environment, it goes a long way to improve the lives of small farmers by providing long-term, stable business ties between coffee producers and coffee distributors [p. 30].’

Price floors and quality

Mr Smith does have one major critique of Henderson (2008) that we accept. Henderson pointed out that the price floors with Fair Trade are not the same as the price floors when government sets them and stands ready to buy the surplus production. With no organisation being willing to buy the surplus, noted Henderson, any surplus would cause the market price to fall. This point is true, but as Smith points out, it is unlikely to be important because market participants are aware of this danger.

Mr Smith writes:

‘Critics of Fair Trade usually argue that as producers will naturally sell the best quality products to open markets, they will dump poor quality goods on Fair Trade co-operatives which are assumed to have no quality controls (Henderson, 2008, p. 63; Sidwell, 2008, p. 14). Again, this view is often a product of theoretical deduction and bereft of empirical

evidence and is again, in my view, rather misleading for those making decisions about the value of Fair Trade.’

Actually, Henderson did cite the paper by Berndt, which contained the evidence. In that paper, she states:

‘While Transfair disputes that Fair Trade coffee is not a high-grade specialty coffee, they acknowledge that farmers do tend to sell the best of the harvest on the open market. Therefore, Fair Trade exposes the industry to free rider problems. When a farmer delivers his Fair Trade coffee beans to the cooperative for milling, they are mixed in with everyone else’s beans. So any advantage in quality he might have is diminished by the quality of the rest of the coffee. Thus, Fair Trade inadvertently encourages mediocrity in production.’

Mr Smith admits in his footnote 14: ‘I have not reviewed the report by C. E. H. Berndt, *Does Fair Trade Coffee Help the Poor?*, as I have not been able to obtain a copy’. Surely Mr Smith’s failure to obtain and read the cited article should not be confused with Henderson’s not having cited evidence.

On a related note, Henderson (2008) drew specifically on the concept of the ‘tragedy of the commons’ (Hardin, 1968), arguing that under Fair Trade, ‘since no one farmer is responsible for the quality of coffee or gets credit for quality, no farmer has a strong incentive to provide quality’. Mr Smith challenges the standard economic analysis of a commons, pointing out that even Hardin admitted that his article ‘should have been called “The Tragedy of the *Unmanaged Commons*.” ’ Mr Smith is correct in saying that the problem with the commons comes about when it is unmanaged – that is, when no one restricts entry or usage. This is a good criticism of the careless version of the ‘tragedy of the commons’ argument, but it is not a valid criticism of the way Henderson (2008) used the argument. In the case of coffee, someone managing a commons to avoid the tragedy would give credit for quality. But, as noted, farmers do not get credit for quality. Thus the tragedy.

Mr Smith writes:

‘When analysis of value and quality are more sophisticated (Raynolds, 2000, p. 306; Zeithaml, 1988), it can be argued that Fair Trade consumers are always getting improved quality given the additional utility derived from social qualities. Instead of externalising everything beyond physical characteristics, a fuller conception of value takes into account the welfare of all stakeholders associated with the product, as well as the “external preferences” of the consumer (Golding and Peattie, 2005, Mann, 2008): i.e. it accepts that even if utility from physical satisfaction “might” (but not necessarily) be less, fulfilment from making a social and environmental contribution cannot be forgotten in analysing how preferences are being met.’

Mr Smith is correct. Again, though, we are seeking to inform people, especially consumers, that some of the benefits that they think they are creating are, in fact, not created. If their subjective evaluation is based on the facts, then the facts we produce are relevant. Indeed, Mr Smith must also think the facts are relevant; otherwise, why would he even discuss them?

Fair Trade and GM

One of the main arguments in Henderson (2008) is that because Fair Trade refuses the option to use

genetically-modified organisms (GMOs), it threatens the existence of bananas, a food that is very important in the diets of many poor people. Mr Smith not only fails to damage Henderson's argument, but also admits key facts that are the building blocks of the argument. He writes:

'As Koepfel (2007) points out, bananas are among the most threatened and disease-vulnerable crops in the world. They are also, by nature of their biology, among the most difficult to conventionally breed. As a consequence, developing a resistant banana by conventional breeding, even if possible, can (and does) take decades. Genetic engineering might cut that time by half, or even more. While this potential has considerable commercial export value, perhaps a more important point is the benefit that these measures could make to populations that depend on bananas for most of their calories – across much of central Africa, for example. For these reasons, Transgenic technology might prove a significant benefit for bananas production, especially given that once bananas have been grown, the prospects for diversification are very limited given the effect that such crops have on the soil.'

This agrees with Henderson (2008). Mr Smith then continues:

'For this reason, there might be grounds to argue that the FLO should critically re-evaluate its current policy, but only where revision is based on comprehensive knowledge and thorough analysis (and this is a view shared by the European Union in maintaining a precautionary approach to such technology).'

This way of thinking – re-evaluate the current policy *only* where it is based on comprehensive knowledge and thorough analysis – is precisely what would lead to the problem that Henderson (2008) pointed out. How would the bureaucracy have comprehensive knowledge? Waiting until the technology is developed is likely to forestall its development. People who make multi-million-dollar investments want to have some assurance that their investment will pay off but they cannot have that assurance if they do not know whether they will be able to sell their product in the market. Depending on a bureaucracy to decide that the knowledge is 'comprehensive' and the analysis is 'thorough' would rightly make many investors nervous. Of course, Mr Smith could argue that too small a percentage of the overall banana crop is produced under Fair Trade to make this a big problem. That is a good argument. But notice that, to the extent that the Fair Traders succeed, it would be a bad argument.

In his conclusion, Mr Smith states that 'it has not been my intention to offer an argument explicitly in favour of Fair Trade'. But he equivocates. In his very next sentence, he writes:

'Overall I would urge those interested in these debates to continue to support Fair Trade while at the same time remaining reflective and critical in their approach – viewing the system as an excellent start in need of reform.'

In other words, he claims that he has not argued in favour of Fair Trade and yet asks us to 'support Fair Trade'. We, however, do not equivocate. We stand behind our case that Fair Trade is not the most efficient way of helping farmers in poor countries.

1. We distinguish Fair Trade, the set of specific business practices ordained by those organisations operating under the umbrella of the Fairtrade Labelling Organization, from the general concept of fair trade as embodying varied interpretations of fairness in business relationships.
2. Berndt interview with Keaton, June 2005.
3. Gerardo Alberto de Leon (Manager, Fedecocagua), in discussion with the author, 6 November, 2006.

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